Media Release:

Taiwan Sugar Corp. Upgraded To 'twAA/twA-1+' On More Stable Profitability; Outlook Stable

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Rating Action Overview

- **Taiwan Sugar Corp.** is a government-owned company operating diversified businesses, mainly in Taiwan, generating revenue of new Taiwan dollar (NT$) 30.2 billion and EBITDA of NT$4.2 billion in 2023. The government directly owns 96% of Taiwan Sugar's shares.
- We acknowledge the improving stability of Taiwan Sugar's profitability and cash flow thanks to its rental-oriented strategy on land-related businesses, as indicated by its growing rental income over the past three years.
- We have raised our long-term issuer credit rating on Taiwan Sugar to 'twAA' from 'twAA-' and affirmed the 'twA-1+' short-term issuer credit rating.
- The stable rating outlook reflects our view that Taiwan Sugar will continue to enhance the stability of its bottom line, supported by the company's gradually improving real estate rental business. The outlook also reflects our expectation of a sustained net cash position over the next two years.

Rating Action Rationale

Rental-oriented strategy on land related businesses is beginning to underpin more stable profitability and cash flow generation. The revenue from Taiwan Sugar's land-related rental income has increased consistently over the past three years with a 42% growth rate over the period. This rental income surpassed revenues from the company's land development and sales business by around NT$ 516 million in 2023. We also view the rental-oriented business model, including such projects as shopping malls, science parks, and export processing areas, and leasing property business have lower inherent risk than for one-off land and property sales.

The success of this business strategy leads us to believe that land-related rental income will remain the majority source of Taiwan Sugar's land-related revenues and could support more predictable profitability and cash flow over the next two years. This somewhat offsets the potential volatility of profitability for the company's agricultural-related businesses.

The performance of agricultural businesses remains largely weak, particularly for its livestock business. Gross profit margin remains stable for the company's sugar business at around 10.5% in 2023. This was up slightly from 10.2% in 2022, supported by a continuous increase in the price of sugar in 2023. However, the gross profit margin of its livestock business remains weaker at negative 4.4% in 2023. This is mainly due to reduced hog volume amid delays in the construction of new pigsties.

However, the profitability of Taiwan Sugar's livestock business could rebound over the next two to three years as more new hog accommodation is built. We expect the volume of hogs to gradually increase to 400,000-450,000 in 2026, from 170,000 at the end of 2023. We expect the economic scale of new hog houses to be around 550,000 once the rebuild is completed.

Financial leverage remains minimal supported by a net cash position. We believe Taiwan Sugar will maintain very low debt leverage over the next two years despite the capital expenditure (capex) needs for pigsty renewal. This will result in negative discretionary cash outflow to support capex before 2026. Several factors support our expectation that Taiwan Sugar will likely maintain a net cash position over the next two years. These include the company's huge land bank that underpins better cash inflow generation on land-related rental business, the company's very low debt usage, and prudent dividend policy.

Outlook

The stable rating outlook reflects our view that Taiwan Sugar could maintain its ratio of debt to EBITDA comfortably below 1.5x over the next two years. The company's equipment-upgrade projects are still ongoing and will increase cash outflow to support capex over the next two years. However, we believe Taiwan Sugar can still meet its capex needs through its large net cash position on hand. In addition, the company's huge low-cost land bank for development and rental business, and very low debt usage support our view of a sustainable net cash position.

Downward scenario

Downside risk for the rating is low over the next one to two years; however, we could lower the rating on Taiwan Sugar if:

1. S&P Global Ratings lowers its issuer credit rating on Taiwan (unsolicited; AA+/Stable/A-1+) by three notches; or
2. The company's profitability is significantly dented as a result of unexpected significant losses, or material volatility of its rental income from land related business; or
3. The management team revises its financial policy in favor of shareholders, such as more capital reduction by increasing financial leverage. A ratio of debt to EBITDA over 1.5x would reflect such activity.

Upward scenario

We believe the potential for an upgrade is limited over the next one to two years; however, we could raise the rating if:

1. The company can significantly improve its revenue base and the profit contribution from its agricultural businesses, or further enhance its rental income streams and contribution from its real estate related businesses, and at the same time,
2. Maintain its ratio of debt to EBITDA below 1.5x.

Our Base-Case Scenario

- Taiwan's real GDP growth at 3.0% as of 2024 and 2.6% in 2025. Sticky inflation might slightly offset the better prices for sugar and hogs due to the higher costs. As the government continues to tighten the housing market, this could constrain growth in Taiwan's housing price.
- The revenue from Taiwan Sugar's land development department will continue to support the company's revenue and profit in 2024-2026, given that there are some construction cases in the pipeline over the next three years. These will help to maintain revenue at the current level in 2024 and possibly grow by 3%-7% in 2025-2026.
- Revenue from property management could grow 5%-7% in 2024 and remain stable in 2025-2026. The rental income from residential houses continues to support the revenue stream from property management. In addition, the rental income from the Lalaport shopping complexes in Taichung and Kaohsiung could support revenue growth over the next two to three years.
- The revenue from sugar business could decrease slightly despite the inflation rate in Taiwan. This is mainly due to the pricing competition from imported sugar products. Also, Taiwan Sugar has a policy role to help the government to stabilize the sugar price, which could lower the margin on its sugar business to 6%-8% in 2024 from 10.2% in 2023.
- Newly renovated hog houses will increase the total volume of pigs to 550,000 once completed. However, construction delays limit the current volume of pigs at around 170,000 at the end of 2023. As construction gradually ends in 2024-2026, hog revenue could increase by 8%-12% in 2024 and 10%-14% in 2025-2026.
- The delay in hog houses renovation will result in capex for these projects of NT$3.6 billion-NT$4.0 billion and NT$2.5 billion-NT$2.9 billion in 2024 and 2025 will be respectively.
- No capital deduction over the next three years.
- Dividend payout will be NT$5.4 billion-NT$5.8 billion in 2024 and NT$1.4 billion-NT$1.8 billion in 2025 respectively.

Taiwan Sugar Corp. -- Forecast Summary

	--Fiscal year ended Dec. 31--					
(Mil. TWD)	**2021a**	**2022a**	**2023a**	**2024e**	**2025f**	**2026f**
Revenue	27,163.9	28,823.6	30,203.2	31,407.7	31,884.9	32,450.7
EBITDA (reported)	2,330.4	2,744.5	3,259.6	2,954.9	3,064.3	3,334.3
Plus/(less): Other	569.9	822.6	907.5	907.5	907.5	907.5
EBITDA	2,900.3	3,567.1	4,167.1	3,862.4	3,971.8	4,241.8
Less: Cash interest paid	(1.0)	(1.3)	(1.8)	--	--	--
Less: Cash taxes paid	(42.6)	(110.0)	(167.5)	(167.5)	(167.5)	(167.5)
Funds from operations (FFO)	2,856.7	3,455.8	3,997.8	3,694.9	3,804.3	4,074.2
Cash flow from operations (CFO)	4,027.6	3,831.7	5,998.6	5,888.2	5,271.4	5,466.6
Capital expenditure (capex)	2,693.5	2,674.0	3,055.7	3,827.4	2,797.4	3,055.7
Free operating cash flow (FOCF)	1,334.1	1,157.7	2,942.9	2,060.9	2,474.1	2,410.9
Debt (reported)	2,353.8	2,045.0	2,175.5	2,175.5	2,175.5	2,175.5
Plus: Lease liabilities debt	168.9	171.7	80.6	37.8	17.7	8.3
Less: Accessible cash and liquid Investments	(40,042.8)	(32,288.4)	(33,325.6)	(30,233.9)	(31,399.5)	(31,402.8)
Debt	--	--	--	--	--	--
Cash and short-term investments (reported)	40,693.9	32,627.7	33,675.8	30,493.1	31,668.7	31,672.0
Adjusted ratios						
Debt/EBITDA (x)	--	--	--	--	--	--
FFO/debt (%)	N.M.	N.M.	N.M.	N.M.	N.M.	N.M.
Annual revenue growth (%)	6.8	6.1	4.8	4.0	1.5	1.8
EBITDA margin (%)	10.7	12.4	13.8	12.3	12.5	13.1
Return on capital (%)	0.8	0.5	1.0	0.8	0.8	0.8

All figures include S&P Global Ratings adjustments' unless stated as reported. N.M.--Not meaningful. a--Actual. e--Estimate. f--Forecast.

Liquidity: Exceptional

The short-term rating on Taiwan Sugar is 'twA-1+'. We assess the company's liquidity as exceptional, given that we believe it has sufficient sources of funds to meet its financial needs up to the end of 2025, supported by its large cash balance on hand and conservative debt usage. The ratio of liquidity sources is likely to be very high at 5.5x-6.0x or more up to the end of 2026.

Our view of the company's liquidity profile incorporates our belief that liquidity sources will continue to exceed uses even if Taiwan Sugar's EBITDA were to decline by 50%. It also reflects our view that the company has prudent risk management and the ability to absorb high-impact, low probability events without financing because of sufficient cash and short-term investment on hand. We also believe Taiwan Sugar has a sound business relationship with banks in Taiwan and a generally high standing in credit markets due to its government owned role. In addition, the company's debt carries no financial covenant.

Principal liquidity sources:

- Cash and short-term investment of NT$31 billion-NT$35 billion in 2024 and NT$27 billion-NT$31 billion in 2025.
- Fund from operations of NT$3.8 billion-NT$4.2 billion in 2024 and 2025.
- Working capital inflow of NT$0.8 billion-NT$1.0 billion in 2024 and NT$0.1 billion-NT$0.3 billion in 2025.

Principal liquidity uses:

- Capex of NT$3.6 billion-NT$4.0 billion in 2024 and NT$2.5 billion-NT$ 2.9 billion in 2025.
- Cash dividend payout of NT$5.4 billion-NT$5.8 billion in 2024 and NT$1.4 billion-NT$1.8 billion in 2025.

Ratings Score Snapshot

Issuer Credit Rating: twAA/Stable/twA-1+

Note: The descriptors below are on a global scale.

Business risk: Fair

- Country risk: Intermediate
- Industry risk: Intermediate
- Competitive position: Fair

Financial risk: Minimal

- Cash flow/Leverage: Minimal

Anchor: twa+

Modifiers

- Diversification/portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Financial policy: Neutral (no impact)
- Liquidity: Exceptional (no impact)
- Management and governance: Neutral (no impact)
- Comparable rating analysis: Neutral (no impact)

Stand-alone credit profile: twa+

- Taiwan's sovereign rating: Unsolicited, rated 'AA+' by S&P Global Ratings
- Likelihood of government support: Moderately high (+2 notches from SACP)

Related Criteria & Research

Related Criteria

- General Criteria: National And Regional Scale Credit Ratings Methodology - June 08, 2023
- Criteria | Corporates | General: Corporate Methodology - January 07, 2024
- Criteria | Corporates | General: Methodology: Management And Governance Credit Factors For Corporate Entities - January 07, 2024
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings - October 10, 2021
- General Criteria: Group Rating Methodology - July 01, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments - April 01, 2019
- Criteria | Corporates | Industrials: Key Credit Factors For The Real Estate Industry - February 26, 2018
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions - March 25, 2015
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers - December 16, 2014
- Criteria | Corporates | Industrials: Key Credit Factors For The Homebuilder And Real Estate Developer Industry - February 03, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions - November 19, 2013
- General Criteria: Methodology: Industry Risk - November 19, 2013
- General Criteria: Principles Of Credit Ratings - February 16, 2011

Related Research

- Taiwan Ratings' Ratings Definitions – November 11, 2021

(Unless otherwise stated, these articles are published on www.taiwanratings.com)

Ratings List

Upgraded

	To	From
Taiwan Sugar Corp.		
Issuer Credit Rating	twAA/Stable/twA-1+	twAA-/Stable/twA-1+

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.taiwanratings.com for further information. Complete ratings information is available to subscribers of Rating Research Service at rrs.taiwanratings.com.tw. All ratings affected by this rating action can be found on Taiwan Ratings' public website at www.taiwanratings.com.